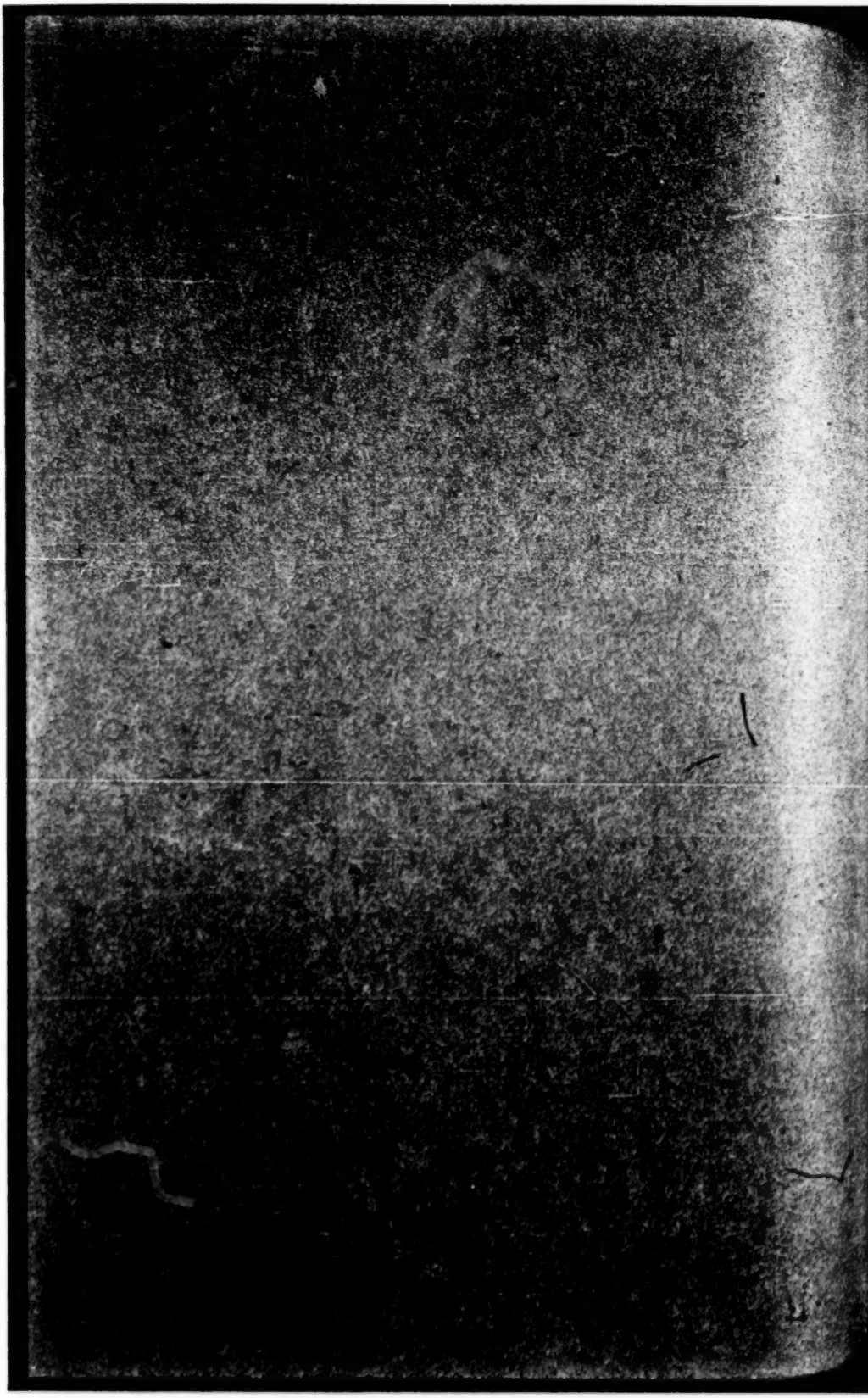

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CHARLES ELMORE CR

IN THE

Supreme Court of the United States,

OCTOBER TERM, 1934.

No. 340

OLD COMPANY'S LEHIGH, INC.,
Petitioner,

against

HENRY E. MEEKER, as Receiver for The First National Bank in Mamaroneck, THE FIRST NATIONAL BANK IN MAMARONECK, and R. G. BREWER, INC.,
Respondents.

BRIEF FOR RESPONDENT MEEKER, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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IN THE

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OCTOBER TERM, 1934.

OLD COMPANY'S LEHIGH, INC.,
Petitioner,

against

HENRY E. MEEKER, as Receiver for The First National Bank in Mamaroneck, THE FIRST NATIONAL BANK IN MAMARONECK, and R. G. BREWER, INC.,
Respondents.

Statement.

Petitioner prays for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit, to review the determination of that court in so far as it affirms the decree of the District Court of the Southern District of New York, dismissing the first two counts of petitioner's amended bill of complaint, for failure to state a cause of action in equity.

Facts.

The allegations of the amended complaint are fairly set forth in the petition and in the opinion of the Circuit Court of Appeals (71 Fed. (2d) 280).

Summary of Argument.

POINT I. The courts below correctly held that Section 350-L, Subdivision 2, of the New York Negotiable Instru-

ments Law, is in conflict with federal law and therefore unenforceable in this case.

POINT II. The courts below correctly held that plaintiff was not entitled to reclamation since the bank's funds were not augmented by the transaction, and no funds belonging to plaintiff came into the receiver's hands.

POINT I.

The courts below correctly held that Section 350-L, Subdivision 2, of the New York Negotiable Instruments Law, is in conflict with federal law and therefore unenforceable in this case.

The first of plaintiff's causes of action is based upon a preference in the distribution of an insolvent bank's assets attempted to be conferred by the New York statute cited, and the second, upon the common law right of a party to reclaim his property in a receiver's hands. In this point, we consider the former of these causes of action, and in the next, the latter.

Section 350-L (2) of the New York Negotiable Instruments Law reads as follows:

> "Except in cases where an item or items is treated as dishonored by nonpayment as provided in section three hundred and fifty-j, when a drawee or payor bank has presented to it for payment an item or items drawn upon or payable by or at such bank and at the time has on deposit to the credit of the maker or drawer an amount equal to such item or items and such drawee or payor shall fail or close for business as above, after having charged such item or items to the account of the maker or drawer thereof or otherwise discharged his liability thereon but without such item or items having been paid or settled for by the drawee or payor either in money or by an unconditional credit given on its books or on the books of any other bank, which has been requested

> or accepted so as to constitute such drawee or payor or other bank debtor therefor, the assets of such drawee or payor shall be impressed with a trust in favor of the owner or owners of such item or items for the amount thereof, or for the balance payable upon a number of items which have been exchanged, and such owner or owners shall be entitled to a preferred claim upon such assets, irrespective of whether the fund representing such item or items can be traced and identified as part of such assets or has been intermingled with or converted into other assets of such failed bank."

It is of decisive importance to note that the relation of trust and the right to priority created by this statute come into operation only when the "drawee or payor shall fail or close for business."

Accordingly, so far as it purports to apply to a national bank, this statute comes directly within the condemnation of this court as expressed in *Davis* vs. *Elmira Savings Bank*, 161 U. S. 275, in running counter to the federal statute (R. S. Sec. 5236; U. S. C. Title 12, Sec. 194) and the inflexible rule thereunder that ratable and equal distribution shall be made in national bank liquidations.

In *Davis* vs. *Elmira Savings Bank*, *supra*, this court said (p. 283):

> "It is clear that these two statutes cover exactly the same subject-matter. Both relate to insolvent banks; both ordain that the right of preference on the one side and the duty of ratable distribution on the other shall duly result from insolvency; both cover the assets of such banks coming, after insolvency, into the hands of the officer or person authorized to administer them It is equally certain that both statutes relate to the same duty on the part of the officer of the insolvent bank; the one directs the representative to make a ratable distribution; the other requires, if necessary the application of the entire assets to payment in full by preference and priority over all others of a particular and selected class of creditors therein named. We have, therefore, on the one hand, the statute of the United States, directing that the assets of an insolvent

national bank shall be distributed by the Comptroller of the Currency in the manner therein pointed out, that is, ratably among the creditors. We have on the other hand, the statute of the State of New York giving a contrary command. To hold that the state statute is operative is to decide that it overrides the plain text of the act of Congress. This results, not only from the fact that the two statutes, as we have said, cover the same subject-matter, and relate to the same duty, but also because there is an absolute repugnancy between their provisions, that is between the ratable distribution, commanded by Congress, and the preferential distribution directed by the law of the State of New York."

At page 287, the court says further:

"It is certain, that in so far as not repugnant to acts of Congress, the contracts and dealings of national banks are left subject to the state law, and upon this undoubted premise, which nothing in this opinion gainsays, the proposition is advanced that the deposit here considered of the Savings Bank with a national bank imported a contract to pay the claim of the former with the preference allowed by the New York statute. But this overlooks the plain terms of the New York law. That statute does not profess to deal with the bank and its relations as a going concern; it wholly and exclusively undertakes to regulate the distribution of the assets after insolvency. Insolvency, and insolvency alone, is made the criterion from which the preference is to arise. Indeed, the statute, in terms directs its mandate to discharge the claim with preference, not to the bank eo nomine, but to the assignee, trustee or agent, charged with administering its effects after insolvency has become flagrant. The claim of contract, therefore, conflicts with the very terms of the statute upon which it is based, and there is, therefore, no room for implying a contract. If such implication, however, could be invoked it must rest on the contention that inasmuch as the state statute gave a savings bank making a deposit the right to be preferred in case of insolvency, therefore the general state law must be presumed to have entered into the contract of the parties, and hence also engender the presumption that in case

of insolvency such deposit should be preferred. If the law of the State is to be read into the contract, then, of course, the law of Congress should also be read into it. We should thus have to consider all the deposits as made with an implication that they were subject to the Federal law, and hence the conflict between the two laws would become evident, and the Federal law, being paramount, would prevail."

See also:

Easton v. *Iowa*, 188 U. S. 220, 238;
Texas & P. R. Co. v. *Pottorff*, 78 L. Ed. 514, 517;
McCandless v. *Dyar*, 34 Fed. (2d) 989
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First National Bank vs. *Selden*, 120 Fed. 212;
Beard vs. *Independent District of Pella City*, 88 Fed. 375;
Palo Alto County vs. *Ulrich*, 199 Iowa 1, 201 N. W. 132.

It should be noted that in cases where no state statute was involved the Federal courts have consistently denied claims for priority on facts similar to those presented in the case at bar.

American Can Co. vs. *Williams* (C. C. A. 2, 1910), 178 Fed. 420;
Wisdom vs. *Keen* (C. C. A. 5, 1934), 69 Fed. (2d) 349;
First National Bank vs. *City of Miami* (C. C. A. 5, 1934), 69 Fed. (2d) 346;
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Larabee Flour Mills Co. v. First National Bank of Dublin, Georgia (D. C. Ga. 1931), 52 Fed. (2d) 146, affirmed 69 Fed (2) 351;

Hirning v. Federal Reserve Bank of Minneapolis, Minnesota (C. C. A. 8, 1931), 52 Fed. (2d) 382;

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Nyssa-Arcadia Drainage District vs. First National Bank (D. C. Oregon, 1925), 3 Fed. (2d) 648.

In *Allied Mills, Inc. v. Horton, supra*, the court said (pp. 710-711):

> "It is a rule of general application in federal courts that where checks on the collecting bank are deposited in the same bank to meet a draft which the bank holds for collection, no trust in the funds thus deposited arises in favor of the drawer of the draft. Hirning v. Federal Reserve Bank (C. C. A. 8) 52 F. (2d) 382, 82 A. L. R. 297 Larabee Flour Mills Co. v. First National Bank of Dublin et al, 52 F. (2d) 146 (D. C.); Larabee Flour Mills v. First National Bank of Henryetta, Okla., 13 F. (2d) 330 (C. C. A. 8); Empire State Surety Co. v. Carroll County et al., 194 F. 593 (C. C. A. 8). The reason

generally assigned in the cases is that in such transactions there is no augmentation of the assets of the bank. There is merely a transfer of existing assets of the bank from one to another.

"If Crisp had brought into the bank the cash wherewith to pay this draft and had paid it in for that specific purpose, the assets of the bank would have been augmented by the cash thus brought in, and a trust might then arise in favor of the drawer of the draft in case the bank fails to pay, and the funds coming into the bank are traceable."

* * * * * * *

"Through the transaction the bank received nothing. Crisp's check depleted his own account in the bank, and the bank's liability for the same amount to the drawer of the draft at once attached. No cash came to the bank. Nothing was taken from or added to its assets."

While the case as bar involves the first and only determination in the Second Circuit construing Section 350-L (2), it is to be noted that the Appellate Division, Second Department of the Supreme Court of the State of New York, in a recent case has similarly construed the same section, likewise holding it to be inconsistent with federal law and therefore inapplicable to an insolvent national bank.

Jones vs. *Board of Education, Town of Pelham*, 242 App. Div. 17.

In that case, the court said (pp. 24, 25):

"It may be that its officers were under the impression that it had a right of preference in the distribution of the assets of the Pelham National Bank by virtue of section 350-l of the Negotiable Instruments Law, added by chapter 589 of the Laws of 1929. If they so believed, they were in error, because there are no preferences among creditors of a national bank. Its assets must be divided ratably among its creditors. (U. S. Code, tit. 12, § 194; Davis v. Elmira Savings Bank, 161 U. S. 275.)"

Petitioner mistakenly argues that the state statute in conferring the preference fixed the relationship of the parties

and granted a lien *ab initio*. Plainly, it does no such thing. It simply lays down the rule to be followed in cases where the collecting bank becomes insolvent. Since that rule is contrary to the federal statutory rule, it can not be enforced in this case.

U. S. Fidelity & Guaranty Co. vs. *National Bank of Americus*, 4 Fed. Supp. 569, upon which petitioner relies, is not inconsistent with the ruling here because (a) the state statute there involved contained no such provision as Section 350 L (2), and (b) the check of plaintiff in that case, drawn on an outside bank, was actually collected by the defendant bank, resulting in the augmentation of its assets traced, into the hands of its receiver. The same result, doubtlessly, would have been reached regardless of the state statute, and consequently the case is of no importance here.

Royal Manufacturing Co. vs. *Spradlin*, 6 Fed. Supp. 98, also relied upon by petitioner, is likewise clearly distinguishable. In that case, the failed bank had issued its draft upon its sufficient account with another bank to pay the collection made by it, and the question was whether that draft was enforceable despite the stop order of the receiver. The state statute (C. S. Supp. N. C. 1924, Sec. 218 C as amended by Pub. Laws 1927, C. 113) created a lien without regard to the solvency of the bank. As the learned court there said (p. 102):

> "The lien exists before insolvency, and subsequent insolvency does not invalidate it."

In the case at bar, as heretofore pointed out, the lien and preference are conferred, by express terms, only in the event of insolvency.

It is further to be noted that the decision of the court in the *Spradlin* case, *supra*, was based largely upon the opinion in *City of Miami* vs. *First National Bank of St. Petersburg*, 58 Fed. (2d) 561, which was practically retracted by the later decision of the same court in the same case *First National Bank of St. Petersburg* vs. *City of Miami*, 69 Fed. (2d) 346.

POINT II.

The courts below correctly held that plaintiff was not entitled to reclamation since the bank's funds were not augmented by the transaction, and no funds belonging to plaintiff came into the receiver's hands.

The general rule, as well established in the federal courts, is that to reclaim property from a receiver the claimant must actually and definitely trace his property into the receiver's hands.

Schuyler v. *Littlefield*, 232 U. S. 707;
Blakey v. *Brinson*, 286 U. S. 254;
Smith v. *Zemurray* (C. C. A. 5 1934), 69 Fed. (2d) 5;
Connolly v. *Lang* (C. C. A. 7 1933), 68 Fed. (2d) 199;
Swan v. *Childrens Home Society of West Virginia* (C. C. A. 4 1933), 67 Fed. (2d) 84;
Harmer v. *Rendleman* (C. C. A. 4 1933), 64 Fed. (2d) 422;
McNair v. *Oesterreicher* (C. C. A. 5 1933) 63 Fed. (2d) 876;
See also cases *supra* (pp. 5, 6).

This, of course, petitioner can not do because the transaction here involved resulted merely in the shifting of credits upon the books of the defendant bank. This fact also confronted petitioner with the further difficulty of inability to prove the fundamental requisite that in the transaction the funds of the bank had been augmented.

See cases *supra*.

To avoid these problems, petitioner resorts to the specious "as if" theory which has been rejected by the federal courts.

Smith v. *Zemurray* (C. C. A. 5—1934), 69 Fed. (2d) 5;
Connolly v. *Lang* (C. C. A. 7—1933), 68 Fed. (2d) 199;
Allied Mills v. *Horton* (C. C. A. 7—1933), 65 Fed. (2d) 708;
McNair v. *Oesterreicher* (C. C. A. 5—1933), 63 Fed. (2d) 876.

In *Connolly* v. *Lang*, *supra*, the court very appropriately said (202):

> "If this were a controversy only between appellee and the bank, there might be good reason for permitting fiction to pervert the facts because all the equities would be with appellee. This action, however, is really between appellee and the general depositors, who without fault on their part have been placed in positions which no doubt are equally deplorable and whose rights to have equity done are equally worthy of consideration."

Petitioner relies upon *Blakey* vs. *Brinson*, 286 U. S. 254, as authority for the approval of the "as if" doctrine, but plainly, Mr. Justice Stone did no more than refer to the theory, without expressing any approval thereof.

Whatever merit the theory may have, it surely should not be applied here where at most there was nothing more than a shifting of credits on the books of the bank. To approve the doctrine under such circumstances would only bring chaos to long established principles of insolvency liquidation. It is significant that whatever adherence the Circuit Court of Appeals of the Fifth Circuit may have appeared to give to the doctrine, has been explicitly and completely retracted in:

Wisdom vs. *Keen*, 69 Fed. (2d) 349;
First National Bank vs. *City of Miami*, 69 Fed. (2d) 346;
Smith vs. *Zemurray*, 69 Fed. (2d) 5.

The petition for a writ of certiorari should therefore be denied.

Respectfully submitted,

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